

Improving Your Retirement System's Controls

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Re-evaluate your system's existing financial
and internal controls

Why?

Why now?

Why not?

Risks

Pre 2012:

- Confident that irregular financial activity would not occur: *It's not worth the risk. Never been worth the risk.*
- Limited degree of probability of such losses.
- Confidence in those we held responsible: *System assets couldn't be at risk?*
- Limited opportunity to take any risk or expose the system to impairment or loss

Controls were compromised

We thought we had:

- *A coordinated system of controls:*
 - *Any controls can be compromised or overridden*
 - *Who is responsible for the system of controls?*
 - *Don't they just get in the way of the way we administer the plan?*

Cash/Bank Account Activity

- Blank check inventory controlled by 1 person
- Checks printed in retirement office for retiree payroll, vendors, transfers, etc.
- Authorized to transfer funds by wire
- Bank statement delivered directly to same person
- Access to facsimile signature to attach to checks

“The Perfect Storm”

- Laptop docking station so the Administrator could “work from home”
- One bank account for all purposes, no file provided to bank
- Warrant did not include actual checks printed, they were done later after approval
- Limited access to actual bank account activity

The Aftermath

- Printed checks payable to a Board Administrator on Quickbooks program at home
- Printed signature of an Assistant Treasurer on same checks
- Deposited checks to a personal bank account
- Reconciled the single bank statement & waited for postman to deliver it!

Undiscovered Theft

- Scheme went undiscovered for nearly 3 years
- Underreported receipts and disbursements on general ledger to cover cash imbalance
- Maintained large cash balance uninvested to cover malfeasance
- “Everybody liked him”, a gregarious, friendly guy

What went wrong? Everything!

- Nobody ever
 - inspected cancelled checks
 - reconciled bank account to actual records of retirement system
 - questioned check order sequence
- Bank had no reason to question his deposits
- Board delegated duty to employee without any oversight

And, there's more

- Transfer of funds by wire never required any justification
- No policy on limits to signature authority, who was authorized?
- No policy on optimal cash balances
- Did not connect with invested cash position
- All deposits were prepared by the Board Administrator, delivered to bank, not recorded in any form of record

Controls should have worked

- Someone other than staff person who prepares the warrant should prepare and print the checks
- Town Treasurer should reconcile bank activity with retirement general ledger
- Town accountant should control check inventory, maintain log record
- Duplicate record of bank deposits kept

What didn't happen?

- Board left the Administrator alone to do his thing
- Complete discretion to perform tasks
- No regular reporting format or agenda
- Budget was an afterthought
- Informal cash position calculation, if any
- Minimal interaction with Investment Manager
- Wire transfers never reported or questioned

What we can do now

- Insist on treasury reconciliation to prove cash, include all reconciling items, no variances or unidentified differences
- Review all cash receipts, disbursements & adjusting journal entries every month
- Match payments to checks, wires, transfers
- Calculate cash position, cover current requirements, determine excess available to invest

Segregating Duties *(For systems with more than one staff person)*

Risks

- A single employee controls all elements of a transaction
- Compensating controls may be inadequate
- Segregating duties and compensating controls are overridden

Controls

- Periodic self-assessment by staff of risk elements
- Rotate functions in high risk areas
- Design management reports that confirm activities
- Authorize an individual to update/confirm wire and/or cash/funds transfer procedures
- Include wire transfers on the warrant so Board can confirm

Systems with one staff person may involve Board Members (ex officio) by frequently reviewing high risk areas.

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Build A Better Budget

- Forecast cash position 12 months in advance
- Compare actual results to the budget by month, year-to-date and 12 months rolling
- Use %'s and positive/negative variances to provide a more visual evaluation
- Insist on a narrative explanation for every variance

Cash Budgeting Risks

- Cash not available when required
- Coordination is lacking between investment and operations
- Lack of formal policy/ procedure to govern process
- Every benefit payroll is a mad rush to fund
- Poor planning causes increased fees

Cash Budgeting Controls

- Priorities are set in written policy manual
- Match disbursements for benefits and operational expenses with receipts from contributions, buy-backs, and appropriations
- Prioritize asset liquidity
- Identify capital calls
- Compare budget to actual expenditures

Payroll Data (Regional Systems)

Risks

- Incorrect compensation and/or contributions are recorded
- Compensation includes disallowed elements
- Contributions not credited properly
- Retroactive adjustments incorrectly applied

Controls

- Provide training and current information to employer units
- Distribute guide or summary of rules, exceptions, and common errors
- Reconcile receipts with contribution reports
- Distribute periodic summary or detail data reports to units and request they reconcile with their records
- Reconcile rates with members' data
- Perform an employer payroll audit
- Send annual statements to members

Don't Ignore Payroll Data

- Many systems include a Housing Authority, RVTHS, RTS, other units
- Contributions can be diverted due to irregular schedule for payments
- Few employees unlikely to match contributions to deductions on W-2
- Many don't confirm with Annual Statement of Contributions

Audit Risks

- Financial information is not useful
- Misstatements, errors, or omissions occur
- Material weaknesses in controls are not identified
- Inadequate affidavit procedures
- Insufficient sampling
- Waste of time/money

Audit Controls

- Compose narrative description of reports
- Reconcile financial information with other sources
- Review Sarbanes/Oxley Act and SAS requirements
- Review work papers
- Assess added value of vendors

Business Continuity Risks

- No disaster recovery plan
- Disaster recovery plan is inadequate
- Plan is not tested, reviewed, or updated
- Key external service providers do not have a plan

Business Continuity Controls

- Develop a plan
- Identify critical processes and assign priorities for recovery within 24, 36, 72 hours
- Develop checklists, procedures, and expected results
- Establish schedule to review and update the plan
- Coordinate with external service providers
- Conduct an actual test

Strategic Planning Risks

- Inadequate planning and documentation
- Inefficient or inappropriate allocation of staff resources
- Failure to complete major projects in a timely fashion

Strategic Planning Controls

- Develop a mission statement, strategic plan, and short and long-term objectives with time frames
- Conduct annual risk assessment and performance review
- Prioritize major projects
- Document existing procedures
- Monitor the plan for compliance

Summary

- Develop a strategic plan
- Develop a plan for business continuity and disaster recovery
- Put all procedures in writing and analyze all functions for vulnerability to fraud and manipulation
- Look for efficiencies without compromising security
- Coordinate budgeting, forecasting, and system funding
- Ensure your system tools work for you and not vice versa
- Provide quality service to all members, retirees, and others
- Keep your investment advisor accountable
- **Identify Risks, Implement Controls**